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SUBJECT: SARKOZY, MERKEL: INTERNATIONAL FINANCIAL COORDINATION  
NEEDS FUNDAMENTAL CHANGE

11. (SBU) Summary: At a January 8-9 "think-in" on capitalism, involving practitioner-politicians and philosopher-economists, President Sarkozy and German Chancellor Merkel said the G20 Summit on April 2nd must set up a new framework of global economic governance to avoid systemic risks in the future. There was broad consensus that a new balance had to be struck between short-term gain and medium- to long-term investment and growth. Furthermore, reform of the 60-year old institutions guiding the international financial system needed to go beyond the Reagan-Thatcher orthodoxy regarding the role of the state in the economy. Ambassador joined a number of GOF Ministers for the opening sessions. End Summary.

Sarkozy and Merkel Call for Fundamental Change  
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12. (U) In a colloquium entitled "New World, New Capitalism" President Sarkozy, German Chancellor Merkel and former British Prime Minister Blair highlighted the need to put capitalism on a new footing and not just "fiddle with" it on the margins. The French and German leaders stressed that this must include adoption of concrete changes at the G20 Summit in London on April 2, including a framework to avoid future crises and regulating activities that pose systemic risks. Sarkozy highlighted national governments are the key actors today and need to coordinate their policies. He warned that while he supported a strong relationship with the U.S., no country could impose its decisions unilaterally. The global economy, he said, was no longer a single currency system. Merkel called for consideration of a UN Economic Security Council with the power to deal with global economic problems comparable to the Security Council's mandate for threats to international peace and security. She also promoted a Charter for the Global Economy with a status like that of the Universal Declaration of Human Rights.

13. (U) The first panel discussion, chaired by Blair, looked at the role of values in bolstering capitalism. Themes were trust/confidence, long-term sustainability and involving stakeholders (vice just shareholders) in private sector decision making. Some participants suggested that laws should impose values, whereas Blair implied that, because of the limits of legal mandates and regulation, values should supplement government actions. Pragmatists such as Nobel Prize economist Amartya Sen asserted that the issue was not a refounding of capitalism but rather a realignment of the role of the state and the market, with the state taking responsibility for social welfare and public goods. Others, including French economist Jean-Paul Fitoussi and Italian Finance Minister Tremonti, echoed President Sarkozy, insisted that

governments need to oblige private - particularly, financial - actors to take into account democratically determined values like long-term growth or social justice. On the issue of America's role and the international system, Francis Fukuyama predicted that America will take a more cooperative approach on the international scene. Former French Prime Minister Rocard and Tremonti seconded this, and also stressed the need for a more coordinated European response to the crisis.

14. (U) The second round table on "Globalization and Justice" was chaired by WTO Director General Pascal Lamy. He stated the scope of the current economic crisis poses new challenges and requires a paradigm shift in how we manage the future of the global economy, rather than tinkering with government oversight or profit and equity issues. In a discussion heavy on rhetorical flourishes critical of the U.S., EU Competition Policy Commissioner Neelie Kroes stressed that "there is no alternative to globalization" and the way forward is to "keep what works and change what doesn't." Dutch Deputy PM and Finance Minister Weuter Bos cautioned that transferring responsibility from national governments to regional or international bodies would have a negative impact on social justice, as only governments can be held accountability for progress or failure. Indian Trade Minister Kamal Nath lamented that what is lacking in globalization is distributive and social justice, highlighting the one billion Indians who earn less than two dollars a day. Professor Joe Stiglitz echoed Nath, giving his critique of the lack of social justice in the U.S. market economy. Lamy concluded by stating a return to the past, of tariffs and protectionism, is not a solution; there is a need to balance the objective of achieving minimal global standards ("an imperative")

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with divergent national/regional models; and an overarching priority of securing a sustainable (by definition, less inequitable and more socially just) approach to international economic growth that engages fully all stakeholders in the global marketplace.

15. (U) The final panel discussion of "How can we regulate capitalism," was chaired by Liberian President Ellen Johnson-Sirleaf who set a positive tone, calling for pragmatic and practical, rather than ideological, solutions to today's challenges. "No one in Africa misses the age of five-year plans, state marketing boards, dual currency regimes and white elephant projects" Both ECB Director Jean-Claude Trichet and former Financial Services Authority Chairman Howard Davies made the point that, financial institutions considered government regulation their biggest risk, prior to the current crisis. It turned out, however, that their own risk management systems had serious shortcomings and they are now happy to accept government funds and guarantees. While these experienced central bankers recommended regulatory changes that improve transparency and discourage procyclical or overly short-term behavior, French labor leader Francois Chereque wanted labor and environmental standards to be considered in financial decisions. Nobel Laureate Edmund Phelps and Czech Central Bank Governor Zdenek Tuma called for careful evaluation of the cost of regulatory measures, lest suppressing "speculation" seriously dampen the dynamism of market capitalism. Phelps questioned the idea of a new capitalism qualitatively different from the 19th century model, and was particularly dismissive of "shareholderism" as a variant on corporatism which supported neither growth nor democracy.

16. (U) In a closing address, Prime Minister Francois Fillon warned that we had come within an inch of a global financial crash. In the future no enterprise, institution or economic actor could be permitted to avoid supervision and regulation in a way that posed systemic risk. Fillon highlighted the strength of Gaullism as an effective approach to safeguarding national, European and global equilibrium. The Gaullist state, he said, has the ability to make long-term strategic decisions (sometimes without oversight or transparency as in the case of France's nuclearization program) and to find the balance between economic efficiency, capitalism and social justice. Fillon also called for medium term engagements between energy producers and energy consumers to stabilize energy prices as well as measures to improve European energy security and address carbon emissions.

17. (SBU) Comment: This colloquium was put together by Eric Besson, State Secretary for Strategic Planning and one of the crossover Socialists recruited by Sarkozy. The program was billed as a followup to a January 2007 think-in at the Sorbonne, also co-hosted with Blair. For Sarkozy, this was an opportunity to close European ranks and especially shore up his German flank, on a reform of "financial capitalism" and to challenge to the United States to work constructively with Europe to move beyond "the status quo" of international finance. As French press commentaries have noted, many here compare the fall of Lehman Brothers to the fall of the Berlin Wall, with both events highlighting the ultimate unsustainability of old approaches in a more and more "globalized" world. If they still seek to goad the U.S. into leadership in ways that suit Europe, they are less than certain they can do the same with emerging economies.

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